

BEFORE THE
PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

PUBLIC UTILITIES
COMMISSION

2009 JUN -9 P 1:30

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In the Matter of the Application of)	
)	
HAWAIIAN ELECTRIC COMPANY, INC.)	DOCKET NO. 2008-0083
)	
For Approval of Rate Increases and)	
Revised Rate Schedules and Rules)	
_____)	

SECOND SET OF REBUTTAL INFORMATION REQUESTS
ON BEHALF OF THE DEPARTMENT OF DEFENSE.

AND

CERTIFICATE OF SERVICE

JAMES N. McCORMICK
Associate Counsel (Code 09C)
Naval Facilities Engineering Command, Pacific
258 Makalapa Drive, Suite 100
Pearl Harbor, HI 96860-3134
Telephone (808) 472-1168

ATTORNEY FOR
DEPARTMENT OF DEFENSE

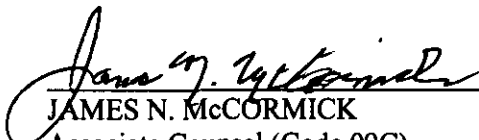
BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

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HAWAIIAN ELECTRIC COMPANY, INC.)	DOCKET NO. 2008-0083
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SECOND SET OF REBUTTAL INFORMATION REQUESTS
ON BEHALF OF THE DEPARTMENT OF DEFENSE.

COMES NOW, DEPARTMENT OF DEFENSE by and through its undersigned attorney
and hereby submits its Second Set of Rebuttal Information Requests to Hawaiian Electric
Company, Inc.

DATED: Honolulu, Hawaii, June 9, 2009.



JAMES N. McCORMICK
Associate Counsel (Code 09C)
Naval Facilities Engineering Command, Pacific
258 Makalapa Drive, Suite 100
Pearl Harbor, HI 96860-3134
Telephone (808) 472-1168

ATTORNEY FOR
DEPARTMENT OF DEFENSE

SECOND SET OF REBUTTAL INFORMATION REQUESTS

TO HAWAIIAN ELECTRIC COMPANY, INC.

QUESTIONS FOR COMPANY WITNESS MORIN

- DOD-RIR-31. For Dr. Morin's updated equity cost estimates please provide the data in electronic spreadsheet format used to support his updated ROE recommendation (e.g., similar to that found in HECO-1901 through HECO-1908 filed with his Direct Testimony).
- DOD-RIR-32. Please explain why Dr. Morin filed no Exhibits with his Rebuttal Testimony.
- DOD-RIR-33. [Ref. Morin Rebuttal, p. 4, ll. 17, 18] Dr. Morin's ROE recommendation for HECO prior to the financial crisis in the Fall of 2008 was 11.25%, subsequent to the financial crisis he finds that an ROE of 11.25% to 11.50% would be reasonable for HECO absent a decoupling mechanism. Please explain how those results support his statement that financial crisis has caused utilities' cost of capital to increase "markedly."
- DOD-RIR-34. [Ref. Morin Rebuttal, p. 6, ll. 3-8]
- a. Please explain why Dr. Morin uses five years of historical allowed return and bond yield data to determine a risk premium, while he used 10 years of data in his Direct Testimony.

- b. What risk premium would be produced by ten years of historical data similar to that shown in the Table on page 6 of Dr. Morin's Rebuttal?
- c. What is the source of the "Average Utility Debt Cost" shown in the table? [Please provide the source for "Average Utility Debt Cost" for the period of 2004 to 2008]

DOD-RIR-35. [Ref. Morin Rebuttal, p. 11] What are the dates at which each of the equity return awards cited were ordered?

DOD-RIR-36. [Ref. Morin Rebuttal, p. 12, ll. 6-8] Please provide the capital cost data comparison between the 1999/2000 period and the current environment supporting Dr. Morin's statement that current capital costs are "at least as high today" as they were during the 1999/2000.

DOD-RIR-37. [Ref. Morin Rebuttal, p. 14, ll. 9-11] Please list any and all electric utilities that have demonstrated long-term average growth in dividends or earnings of 6.3% to 7.3%, as well as supporting data for any listed. If Dr. Morin is unable to identify any such utilities, please explain why it is reasonable to believe that investors expect AEP to grow indefinitely in the future at that rate.

DOD-RIR-38. [Ref. Morin Rebuttal, p. 15, ll. 15-17]

- a. Please define "scientific foundation" as used in the cited portion of Dr. Morin's Rebuttal testimony and please explain in detail how the use of historical and projected growth rates in earnings,

dividends and book value lacks such “scientific foundation” in cost of equity estimation.

- b. Are historical and projected growth rates in earnings, dividends and book value listed in Dr. Morin’s text considered as possible means to estimate investors’ expected long-term growth rate in a DCF analysis?

DOD-RIR-39. [Ref. Morin Rebuttal, p. 16, ll. 18-21] Please provide cites for the literature referenced.

DOD-RIR-40. [Ref. Morin Rebuttal, p. 17, ll. 6-7] Please provide the data on which Dr. Morin bases his statement that the use of average common equity balances in calculating a return on equity is “common regulatory practice.”

DOD-RIR-41. [Ref. Morin Rebuttal, p. 17, ll. 16-18] Please provide the analysis undertaken by Dr. Morin to support the statement cited.

DOD-RIR-42. [Ref. Morin Rebuttal, p. 18, ll. 12-15] Please explain why Dr. Morin believes that Value Line growth forecasts are not representative of investor expectations for long-term dividend growth while he believes Value Line’s betas are representative of investors’ perceptions of relative risk and expected return (based on his reliance on Value Line’s published betas in his CAPM analysis).

DOD-RIR-43. [Ref. Morin Rebuttal, p. 20, l. 3] Please provide a complete copy of the Timme and Eisemann article cited in footnote 2.

DOD-RIR-44. [Ref. Morin Rebuttal, p. 22, ll. 13-16]

- a. Please provide the source documents from which the Blue Chip forecast of 5.1% GDP and the “administration” forecast of 4.9% GDP were drawn by Dr. Morin.
- b. What would Mr. Hill’s two-stage DCF result have been with a 5.1% GDP growth rate and what would it have been with a 4.9% growth rate? If Dr. Morin is unable to provide a response to this question, please explain why.

DOD-RIR-45. [Ref. Morin Rebuttal, p. 22, ll. 17-21]

- a. Please explain why it is necessary for Mr. Hill to compare historical GDP growth with current GDP growth expectations in a multi-stage DCF, while it is not appropriate, in Dr. Morin’s opinion, to compare historical growth with current projections in a standard DCF analysis.
- b. Please provide the source document for Dr. Morin’s cited estimate of a 3.5% long-term forecast of real growth for GDP (footnote 4).
- c. Please explain why a ten-year projection of GDP is not appropriate as an assumption of long-term growth for the DCF while a 5-year projections of earnings per share for an electric utility is appropriate.

DOD-RIR-46. [Ref. Morin Rebuttal, p. 23, 3-11]

- a. Does the 10.92% figure cited include the addition of a 30 basis point upward adjustment for flotation costs? If not, please provide an explanation of the manner in which the calculation of the 10.92% was determined.
- b. Is it true that, using the two-stage DCF model used by Mr. Hill, the use of a 5.5% GDP estimate as the long-term growth rate produces a DCF estimate of 10.62%? If not, please explain why not.

DOD-RIR-47. [Ref. Morin Rebuttal, p. 25, ll. 7-10] Is it Dr. Morin's testimony that the cost of capital for utilities is, at all times, equal to the allowed return? If so, why do market prices diverge from book value?

DOD-RIR-48. [Ref. Morin Rebuttal, p. 26, l. 5] If Dr. Morin believes that the CAPM is less reliable than the DCF, please explain why he has elected, after publishing two editions of his cost of capital textbook in which the DCF model is presented as the initial cost of equity model, to feature the CAPM as the first equity cost model in his most recent textbook. That is if Dr. Morin believes the CAPM is inferior, why make such a dramatic change in his textbook on the subject?

DOD-RIR-49. [Ref. Morin Rebuttal, p. 26, ll. 12-14] Dr. Morin notes that the beta coefficients of his electric utilities have declined since he filed his Direct Testimony. Given that Value Line betas are

determined over a five-year historical period and, following the crisis, they have declined, does that mean that the economic crisis caused the decline in betas? If not, please explain why not.

- DOD-RIR-50. [Ref. Morin Rebuttal, p. 26, l. 22] Does Dr. Morin believe that the market prices of U.S. Government bonds are not “market prices?” If so, why; if not, please affirm that T-Bond prices are determined in the market.
- DOD-RIR-51. [Ref. Morin Rebuttal, p. 30, ll. 17-19] Please provide support for Dr. Morin’s contention that the amount of funds booked as a result of the sale of an original-issue utility bond is equal to the money actually put up by the investor.
- DOD-RIR-52. [Ref. Morin Rebuttal , p. 31, l. 23] Please explain why Dr. Morin believes research published by the National Regulatory Research Institute is “obscure.”
- DOD-RIR-53. [Ref. Morin Rebuttal, p. 33, ll. 15-19] Has Dr. Morin performed any study to compare and contrast the type of adjustment clauses, ROE incentive riders, trackers, and recovery mechanisms enjoyed by his sample group of companies with those contemplated in HECO’s Energy Agreement? If so, please provide a complete copy of any such study or analysis.
- DOD-RIR-54. [Ref. Morin Rebuttal, p. 36, ll. 7-14] Please explain how a 9.62% return on market value would equal a 5.06% return on

book value if the market value is 1.9 times the book value. If a 9.62% return on market value and a market-to-book ratio of 1.9 does not equate to a return of 5.06% on book value, please so state.

DOD-RIR-55. [Ref. Morin Rebuttal, p. 36, ll. 29-31]

a. Does “conservative” mean “too low” in the cited portion of Dr. Morin’s testimony? If not, please provide the appropriate definition in context.

b. Please provide the GAAP guidelines to which Dr. Morin refers.

DOD-RIR-56. [Ref. Morin Rebuttal, p. 37, ll. 3-7] Please cite to any long-term forecasts of pension fund returns that utilize arithmetic averages.

DOD-RIR-57. [Ref. Morin Rebuttal, p. 37, l. 10] Is it true that DCF, CAPM and Risk Premium equity cost estimation methods produce estimates of market-required returns? If not, please explain why not and provide support for your response.

DOD-RIR-58. [Ref. Morin Rebuttal, p. 37, ll. 11-22]

a. Is it Dr. Morin’s testimony that all market-based equity cost estimation methods (DCF, CAPM, Risk Premium) understate the cost of equity when market prices are above book value and overstate the cost of equity when market prices are below book value? If not, please explain why not.

- b. Please provide any cost of capital testimony submitted by Dr. Morin within the past five years in which he has estimated the cost of equity of an electric utility with a market price above book value and made an explicit upward adjustment to his CAPM, Risk Premium and DCF results to account for the difference between market price and book value.
- c. Does the cited portion of Dr. Morin's testimony conflict with his published statements on the application of market-based equity costs to book-value rate base? If so, why; if not, please explain why not.

DOD-RIR-59. [Ref. Morin Rebuttal, p. 43, l. 17] Please define what is meant by "grossed up" in the cited portion of Dr. Morin's testimony.

DOD-RIR-60. [Ref. Morin Rebuttal, p. 47] Please provide complete copies of each of the articles cited in the footnotes at the bottom of page 47.

DOD-RIR-61. [Ref. Morin Rebuttal, p. 70, ll. 10-17]

- a. Please explain how the financial crisis in 2008 affected the reliability of Dr. Morin's Moody's Electric Utility Index data. That is if the Moody's utility index publication was discontinued in 2002, and Dr. Morin relied on it in 2008 in his Direct Testimony, why would the financial crisis affect its reliability?

- b. If Dr. Morin had continued to rely on the Moody's Index companies in his update of the cost of equity, what would his risk premium result have been? Please provide supporting data.
- c. Please list the companies included in the Moody's Index used by Dr. Morin in his Direct Testimony and list the companies included in the S&P Index used in his update.

DOD-RIR-62. [Ref. Morin Rebuttal, p. 70, ll. 18-22]

- a. If Dr. Morin had used government bond yields in his risk premium analysis in his update, as he did in his Direct Testimony, what would have been the result?
- b. If government bond yields do not "directly capture" trends in utility cost of capital, please explain why Dr. Morin used government bond yields to estimate the cost of utility common equity in his direct testimony in this proceeding.
- c. Please provide a complete copy of any testimony in the past five years prior to 2009 submitted by Dr. Morin in which he has used utility bond yields instead of government bond yields in his risk premium analysis.

DOD-RIR-63. [Ref. Morin Rebuttal, p. 71, ll. 12-13]

- a. If Dr. Morin had utilized the same allowed return risk premium method that he used in his Direct Testimony, what would have been the result?

- b. Please affirm that the allowed return risk premium method used by Dr. Morin in his Direct Testimony is based on the past ten years of data.
- c. Please explain why “the scarcity of decisions” in late 2008 would cause an analysis which also included ten years of historical data to be rendered invalid.
- d. How many rate case decisions were rendered in the 4th quarter of 2008 versus the 4th quarter of each of the past 10 years? Please provide supporting data.

DOD-RIR-64. [Ref. Morin Rebuttal, p. 71, ll. 15-22]

- a. Are the companies used in the two electric utility groups in Dr. Morin’s Rebuttal update the same companies that were used in his two electric utility groups in his Direct Testimony? If not, please explain why not.
- b. Please list the companies in Dr. Morin’s two sample groups used in his updated cost of equity estimate.

CERTIFICATE OF SERVICE

I hereby certify that one copy of the foregoing document was duly served upon the following parties, by personal service, hand-delivery, and/or U.S. mail, postage prepaid, and properly addressed pursuant to HAR sec. 6-61-21(d).

Ms. Catherine P. Awakuni
Executive Director
Division of Consumer Advocacy
Department of Commerce and Consumer Affairs
P. O. Box 541
Honolulu, HI 96809

2 Copies

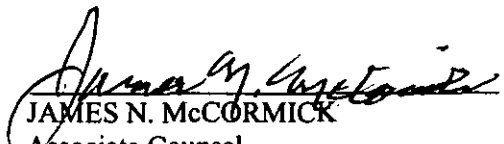
Darcy L. Endo-Omoto
Vice President - Government and Community Affairs
Hawaiian Electric Company, Inc.
P. O. Box 2750
Honolulu, HI 96840-0001

Mr. Dean K. Matsuura
Manager - Regulatory Affairs
Hawaiian Electric Company, Inc.
P. O. Box 2750
Honolulu, HI 96840-0001

Thomas W. Williams, Jr., Esq.
Peter Y. Kikuta, Esq.
Damon L. Schmidt, Esq.
Goodsill Anderson Quinn & Stifel
Alii Place, Suite 1800
1099 Alakea Street
Honolulu, HI 96813

Counsel for Hawaiian Electric Company, Inc.

DATED: June 9, 2009, Honolulu, Hawaii


JAMES N. McCORMICK
Associate Counsel
Naval Facilities Engineering Command,
Pacific